MOTION FILED
AUG 18 1977

No. 76-1359

IN THE

Supreme Court of the United States

October Term, 1976

BANKERS TRUST COMPANY,
Petitioner,

v.

SAMUEL MALLIS and FRANKLYN KUPFERMAN,
Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

MOTION AND BRIEF OF THE NEW YORK CLEARING HOUSE ASSOCIATION, *AMICUS CURIAE*

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MOTION OF THE NEW YORK CLEARING HOUSE ASSOCIATION FOR LEAVE TO FILE A BRIEF AS *AMICUS CURIAE*

The New York Clearing House Association hereby moves pursuant to Rule 42 of this Court for leave to file a brief as *amicus curiae* urging reversal of the decision of the court of appeals. This motion is necessitated by the refusal of respondents Mallis and Kupferman to consent to the filing of the Association's brief.

The New York Clearing House Association, founded in 1853, is an association of eleven leading commercial banks in the City of New York.[1] The Association clears commercial drafts and items in the New York area and,

[1] The Bank of New York, The Chase Manhattan Bank, N.A., Citibank, N.A., Chemical Bank, Morgan Guaranty Trust Company of New York, Manufacturers Hanover Trust Company, Irving Trust Company, Bankers Trust Company, Marine Midland Bank, United States Trust Company of New York and National Bank of North America.

through its counsel, files briefs before courts of appellate jurisdiction in cases which raise significant questions of law relating to banking.

In the decision below, the court of appeals held that a pledge of stock as security for the repayment of a commercial loan, and the release of such a pledge upon repayment, each constituted a "purchase or sale" of the pledged stock within the meaning of § 10(b) of the Securities Exchange Act of 1934. The decision imposes a general federal antifraud provision upon all commercial loan transactions that are collateralized by securities and thereby supersedes the legal structure governing security interests that has evolved from the common law and statutory draftsmen over hundreds of years.

The New York Clearing House Association, which represents banks with over $6 billion in loans collateralized by securities, believes the decision below was error for the reasons set forth in the accompanying brief. The Association thus respectfully prays that the Court grant this motion for leave to file its brief.

Respectfully submitted,

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BRIEF OF THE NEW YORK CLEARING HOUSE ASSOCIATION, *AMICUS CURIAE*

The New York Clearing House Association, *amicus curiae*, submits this brief on an issue of importance to the commercial banking system: Whether a pledge of stock as security for the repayment of a commercial loan, and the release of such a pledge upon repayment, are each a "purchase or sale" of the pledged stock within the meaning of § 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b).

The Court of Appeals for the Second Circuit (per Timbers, J.) held that both a pledge and the release of a pledge constitute such a "purchase or sale" and, con-

sequently, that § 10(b) governs all loan transactions where securities are put up as collateral. This holding is contrary to the language and purpose of the statute, is based upon a fundamental misconception of the nature and consequences of a pledge, and is unsound as a matter of public policy.

Statement of the Case

The facts of this case are detailed fully in the opinions of the courts below. In short, respondents Mallis and Kupferman ("plaintiffs") borrowed $156,000 from Franklin National Bank and reloaned the money to a Mr. Arnold, for a payment of $50,000.[1] Arnold used the proceeds to purchase certain stock certificates purporting to represent an interest in Equity National Industries. The certificates, which Arnold pledged to plaintiffs as security for their loan, apparently proved worthless and Arnold did not repay plaintiffs. Plaintiffs in turn refused to repay their debt to Franklin National Bank. (A129-30; 156-58)

The connection of Bankers Trust Company ("Bankers Trust") to this series of transactions was that the certificates had previously been pledged to it as collateral for a loan to Arnold's seller, a Mr. Kates. Bankers Trust returned the certificates to Kates when, at a simultaneous closing, Kates sold the certificates to Arnold and repaid Bankers Trust with a portion of the proceeds from the sale. (A130-31; 156-58)

[1] Plaintiffs' extension of credit to Arnold for a 30-day period in consideration of a payment of $50,000 appears to have violated the New York criminal usury law. N.Y. PEN. LAW § 190.40 (McKinney Supp. 1976).

Plaintiffs have alleged that Bankers Trust knew when it released the certificates from pledge that they were worthless and apparently contend that Bankers Trust is thereby *ipso facto* liable under § 10(b) to them as subsequent pledgees of the certificates. Plaintiffs also claimed below that they had no obligation to repay their loan from Franklin National Bank because the transaction violated Regulation U, 12 C.F.R. Part 221, promulgated under § 7 of the 1934 Act, 15 U.S.C. § 78g, which regulates the extension of credit for the purpose of "purchasing or carrying" securities.

The district court (Pollack, J.), citing *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723 (1975), held that plaintiffs were not "purchasers" of securities and that their action therefore did not state a claim against Bankers Trust under § 10(b) of the 1934 Act (A134). Judge Pollack also held that plaintiffs could not invoke Regulation U to avoid their obligation to Franklin National Bank (A131-33).

The court of appeals reversed as to Bankers Trust, holding that plaintiffs' acceptance of Arnold's pledge was a "purchase" of securities under § 10(b) of the 1934 Act, and also that "Bankers Trust was a seller by virtue of its release of the Kateses' pledge", *i.e.*, that the termination of a pledge is a "sale" (A162-65). The court of appeals affirmed plaintiffs' obligation to repay the loan from Franklin National Bank, however, holding that Regulation U was inapplicable because plaintiffs were not "purchasing" any securities as required by § 7(a) of the 1934 Act (A161). The court of appeals did not attempt to reconcile its conflicting definitions of "purchase" under the 1934 Act.

ARGUMENT

I.

Pledge Transactions Are Not Within the Express Scope of § 10(b) of the 1934 Act.

In rejecting recent attempts to expand the coverage of § 10(b), the Court has noted that "[t]he starting point in every case involving construction of a statute is the language itself." *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 197 (1976); *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 756 (1975) (Powell, J., concurring). The language should be read according to "its commonly accepted meaning," *Ernst & Ernst* v. *Hochfelder*, *supra* at 199, and is " 'to be understood according to the sense of the thing, as the ordinary man has a right to rely on ordinary words addressed to him,' " *id.* at n. 19, quoting *Addison* v. *Holly Hill Fruit Products, Inc.*, 322 U.S. 607, 617-18 (1944).

Section 10(b) of the 1934 Act and Rule 10b-5 thereunder apply by their terms to the "purchase or sale" of securities and only to such transactions. *See Blue Chip Stamps, supra.* "Purchase" and "sale" are "ordinary words," *see SEC* v. *Sterling Precision Corp.*, 393 F.2d 214, 217-18 (2d Cir. 1968) (Friendly, J.), and are thus to be construed according to their "commonly accepted" meanings. *See id.*, (" 'Purchase' is not a peculiarly technical term"); *Blue Chip Stamps, supra* at 756 (Powell, J., concurring) ("sale" has a "long-established legal meaning" applicable under § 10(b)).

A "sale" is a "contract whereby the absolute, or general, ownership of property is transferred from one person to another for a price, or sum of money, or, loosely, for any consideration." WEBSTER'S INTERNATIONAL DICTIONARY (2d ed. 1934). A "purchase" is an "acquisition of title to, or property in, anything for a price; buying for money or its equivalent." *Id.*

The definitional section of the 1934 Act, § 3(a), 15 U.S.C. § 78c(a), does not alter these "commonly accepted" meanings except to make it clear that executory as well as fully executed contracts of purchase and sale are included:

> "(13) The terms 'buy' and 'purchase' each include any contract to buy, purchase, or otherwise acquire.
>
> (14) The terms 'sale' and 'sell' each include any contract to sell or otherwise dispose of."

See Blue Chip Stamps, supra at 750-51. The correlative terms "otherwise acquire" and "otherwise dispose of" are not referred to in the legislative history, but seem to have the effect of including transfers of ownership through barter or in exchange for services, which do not involve, in the strict dictionary sense, a "price" or "money or its equivalent." These terms do not, in any event, derogate from the basic point that "purchase" and "sale" mean the acquisition and disposition of ownership; indeed, they confirm it.

A pledge of securities or other property as collateral for a loan, and the acceptance of such a pledge, do not fall within the "commonly accepted" meanings of "sale" and "purchase" because no title or ownership is passed from pledgor to pledgee. This is true *a fortiori* of the release of a pledge. A pledge does not transfer (or "dispose of") ownership, but creates an entirely different interest, long known to and regulated by the law as a security interest. The release of a pledge does not pass any interest from or to anyone; it simply extinguishes the security interest created by the pledge. These distinctions are matters of both common understanding and legal substance.

A pledge is "a deposit of personal property as security, with an implied power of sale upon default," or a

" 'bailment of goods by a debtor to his creditor to be kept till the debt be discharged.' " L. JONES, COLLATERAL SECURITIES AND PLEDGES § 1 (3d ed. 1912); *accord*, RESTATEMENT OF SECURITY § 1 (1941). Pledgees have "no general property right in the thing pledged, but only a right, upon default, to sell in satisfaction of the pledgor's obligation," and even third parties "cannot regard a pledgee as the actual owner." *Pauly* v. *State Loan & Trust Co.*, 165 U.S. 606, 622 (1897). *See also Burgess* v. *Seligman*, 107 U.S. 20, 29, 37 (1882) ("mere pledgee" contrasted with "true owner"); L. JONES, *supra* § 602.

The physical re-delivery or "release" of the pledged property upon repayment of the secured obligation is not a voluntary act, but a legal duty. The pledgee's security interest in the pledged property is extinguished by operation of law, and the release is not a transfer of ownership, which was never in the pledgee, but a natural consequence of that extinction. L. JONES, *supra* §§ 540, 544; RESTATEMENT OF SECURITY § 37; *see* U.C.C. 9-506.

Even upon default, a pledgee has no right or option to sell the collateral for its own account, but only for the account of the pledgor. *Easton* v. *German-American Bank*, 127 U.S. 532, 537 (1888):

> "In reference to the pledge and to the pledgor, [the pledgee] occupies a fiduciary relation, by virtue of which it becomes his duty to exercise his right of sale for the benefit of the pledgor."

The pledgee must sell the collateral in a "commercially reasonable" manner, U.C.C. § 9-504(3); *see* L. JONES, *supra* § 602; RESTATEMENT OF SECURITY § 49, and must account in such a sale for all proceeds in excess of the debt, U.C.C. § 9-504(2), and for all profits accruing as a result of possession of the collateral. RESTATEMENT OF SECURITY § 27; *Burgess* v. *Seligman*, *supra* at 29. The pledgee may always collect on the note, either instead of realizing on

the collateral or if the proceeds from sale are insufficient. L. JONES, *supra* §§ 590, 597; RESTATEMENT OF SECURITY § 48.

Nor does a pledge of stock carry any other of the important indicia of ownership. Taxes incident to stock ownership are payable by the pledgor, L. JONES, *supra* § 176a, and the pledgor normally has the right to vote the stock, *id.* at § 441; *cf. Burgess* v. *Seligman*, *supra*. Pledgees are immune from liability as stockholders, *Pauly* v. *State Loan & Trust Co.*, *supra*; L. JONES, *supra* §§ 445-456. Pledgees at common law are even prohibited from purchasing the pledged property upon default absent supervision by a court or agreement by the pledgor. L. JONES, *supra* § 635; RESTATEMENT OF SECURITY § 51; *Easton* v. *German-American Bank*, *supra* (a pledgee "is by a familiar maxim of equity forbidden to purchase for his own use at his own sale."). *Cf.* U.C.C. § 9-504(3).

Thus, a pledgee is but a lender-bailee with a contractual right to repayment of the debt to which the pledged security is "collateral," as well as a contingent right, if the pledgor defaults on the loan, to act as a sales agent for the pledgor and to receive a fixed sum out of the proceeds. The SEC's rules under the 1934 Act are in accord with the common law, and recognize that the pledgee is in effect a custodian of the stock for the pledgor and has no ownership interest.[3]

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[3] Rule 16a-6, 17 C.F.R. § 240.16a-6, which governs stock ownership filings by corporate insiders, expressly notes that a pledge of stock is not a transfer of a security and, indeed, does not constitute any "put, call, option or other right or obligation to buy . . . or sell securities":

> "2. The right of a pledgee or borrower of securities to sell the pledged or borrowed securities is not an option or right to sell securities within the meaning of this section. However, the sale of the pledged or borrowed securities by the pledgee or borrower shall be reported by the pledgor or lender."

Rule 16a-6 thus requires that the sale out of pledge be considered a transfer by the pledgor, who must make appropriate ownership filings, not a transfer by the pledgee, who is not the owner.

In sum, neither a pledge of stock as security for a loan nor the release of such a pledge upon repayment is a "purchase or sale" of the stock in the realities of commerce or within the meaning of the 1934 Act. Simple definitional analysis and established canons of statutory construction require reversal of the holding below. While the clarity of the statutory language renders further inquiry unnecessary, *see Ernst & Ernst* v. *Hochfelder*, *supra* at 201; *United States* v. *Oregon*, 366 U.S. 643, 648 (1961), an analysis of congressional purpose and policy considerations also requires reversal.

II.

Congressional Purpose and Sound Policy Confirm that There Is No Warrant for Judicial Extension of § 10(b) to Pledge Transactions.

The language of a statute is presumed to have its ordinary meaning, and a party asserting otherwise must make a clear showing that the legislation requires a different interpretation. As expressed by Judge Friendly in *SEC* v. *Sterling Precision Corp.*, 393 F.2d at 218:

> "A party asserting that a word in a statute should be given a meaning different from what it has in the speech of common men or, in this instance, the common speech of lawyers, has the burden of showing that context or evident p[illegible]se requires this."

Here, both the "evident purpose" of the 1934 Act and its general legislative context confirm the presumption that the words "purchase" and "sale" are to be given their "commonly accepted" meanings.

The 1934 Act was not intended to establish a federal commercial law, but rather to provide relief for particular problems of the investing public. *See Santa Fe Industries*

v. *Green*, 97 S. Ct. 1292, 1303-04 (1977). The Act was "chiefly concerned with the regulation of post-distribution trading on the Nation's stock exchanges and securities trading markets." *Blue Chip Stamps*, *supra* at 752; *see id.* at 728.

The pledgor-pledgee relationship involves no use of stock exchanges and has no effect on trading markets. The stock markets are involved only if the pledged securities are sold upon default, and such sales are, of course, subject to § 10(b)'s proscriptions as between the purchaser, on the one hand, and the pledgor and his agent, the pledgee, on the other.

Nor was there any need for Congress to extend § 10(b) to pledges in order to effectuate its antifraud purposes. The parties to a pledge transaction are situated quite differently from purchasers and sellers of securities in terms of legal recourse under state law. In the event that the pledgor fails to repay the loan and the pledged securities prove to be worthless, the pledgee need not resort to a common-law fraud action. He has a direct and simple action against the pledgor on the unpaid note. And a pledgor, unlike a seller of securities, cannot be the victim of any securities fraud by the pledgee, because the stock, or its proceeds, still belongs to the pledgor. Misappropriation of the collateral by a pledgee in possession is no more a securities fraud than would be a robbery of a brokerage house. The pledgor simply maintains a straightforward action for conversion.[8]

The purpose of Congress in enacting § 10(b) thus had nothing to do with regulating pledge transactions. It is clear as well that Congress enacted the various securities legislation of the 1930's to accomplish specific objectives, and when Congress needed to impose special definitions

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[8] *See Meisel* v. *North Jersey Trust Co.*, 218 F.Supp. 274, 278 (S.D.N.Y. 1963).

upon common words in order to attain these objectives, it did so. In the Public Utility Holding Company Act of 1935, for example, Congress prescribed a broad definition of "sale" specifically to include pledges as well as leases. 15 U.S.C. § 79b(a)(23). In that Act Congress sought to regulate all substantive business transactions among utility affiliates and holding companies to avoid manipulation of profits and losses, *see, e.g.*, 15 U.S.C. § 79*l*, and chose its language to that end. In the 1934 Act, on the other hand, Congress regulated securities trading, not a broad range of commercial transactions, and required no more than the "commonly accepted" definitions of "purchase" and "sale" to achieve fully its purposes.

In declining to construe "sale" under § 10(b) to include offers to sell, the Court in *Blue Chip Stamps* contrasted § 10(b) with § 17(a) of the 1933 Act, which expressly includes both the "offer" and "sale" of securities. *Id.* at 733-34 & n. 5; *id.* at 756. The contrast between the definitions of "sale" in the 1934 Act and in the Public Utility Holding Company Act of 1935 similarly precludes judicial substitution of the latter's broad definition in the 1934 Act, which is a "carefully drawn statute [that] itself defines the term 'sale.'" *Id.* at 733 n. 5.

Congress by the 1934 Act did not seek to regulate commercial loans, and there is no basis for distinguishing unsecured loans from secured loans, whatever the collateral. As Professor Loss aptly has noted, "federal legislation was hardly needed for privately negotiated pledge transactions between borrowers and lenders." 1 L. LOSS, SECURITIES REGULATION 649 (2d ed. 1961).

The inevitable consequence of extending the scope of § 10(b) to pledge transactions would be a rash of vexatious litigation by borrower-pledgors seeking any means

possible to avoid financial reversals.[4] The delay value alone of such frivolous actions, where the plaintiffs would be freed from the constraints of the statute of frauds and other proven limitations under state law, would be substantial, without any corresponding increase in protection afforded the parties to the pledge transactions. *See Blue Chip Stamps, supra* at 741. The adjudication of such claims, which are totally devoid of any connecting link with the securities laws, would be a vast waste of judicial energy. The defense of such actions would likewise impose an unnecessary and costly burden on lending institutions and thereby restrict the availability of credit or add to its cost.

If the legal regime governing commercial loans, which evolved from the common law and statutory draftsmen over hundreds of years, is to have a divergent provision of federal law such as § 10(b) superimposed upon it, that decision should be made by Congress, not the courts.

III.

The Decision Below Was Unsupported by Reasoned Analysis.

The court below ignored this Court's teachings as to statutory construction by failing to accord the terms "purchase" and "sale" their "commonly accepted" mean-

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[4] Among the claims that pledgors have sought to assert under § 10(b) are that the pledgee promised that the pledgor-borrower could have time to find a purchaser for the collateral, *Dopp* v. *Franklin National Bank*, 461 F.2d 873 (2d Cir. 1972); that the pledge was induced through misrepresentations, *McClure* v. *First National Bank of Lubbock, Texas*, 497 F.2d 490 (5th Cir. 1974), *cert. denied*, 420 U.S. 930 (1975); that the issuer reneged on a promise to register the shares so as to maximize the proceeds on a default sale, *Devonbrook, Inc.* v. *Lily Lynn, Inc.*, [1973-1974 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 94,621 (S.D.N.Y. 1974); that the pledgee made an unfair loan to the pledgor to the detriment of the guarantor, *Woodward* v. *Metro Bank of Dallas*, 522 F.2d 84 (5th Cir. 1975).

ings. Its only apparent reason for doing so was its erroneous postulate, adopted from an earlier decision under § 17(a) of the Securities Act of 1933, that pledgees assume an " 'investment risk . . . identical in nature to the risk taken by investors' " (A163, quoting *United States* v. *Gentile*, discussed at pp. 14-15, *infra*).[5]

Contrary to the conclusion of the court below, a pledgee is a lender, with recourse against all the pledgor's assets, not an "investor" in specific assets. The pledge of stock as security for a loan is truly "collateral" to the loan transaction, and does not transform the loan into a securities investment any more than the acceptance of a pledge of receivables from a retailer places a commercial lender in the business of retailing. Far from assuming an "identical" "investment risk," the pledgee receives no benefit from appreciation of a security, and his risk from depreciation does not affect the right to repayment but is merely one of numerous factors, the most important of which is the pledgor's overall financial condition, which affect the ease of repayment.[6]

In support of its holding the court of appeals cited two cases decided under the Securities Act of 1933, *SEC* v. *Guild Films Co.*, 279 F.2d 485 (2d Cir.), *cert. denied*, 364 U.S. 819 (1960) and *United States* v. *Gentile*, 530 F.2d 461 (2d Cir.), *cert. denied*, 426 U.S. 936 (1976), which had broadly opined that all pledges were "sales" under that Act. Neither of these decisions provides more solid

[5] In an effort to distinguish *Blue Chip Stamps*, the court also stated that a "pledge . . . is just as concrete a transaction as is a normal transfer of title" (A164). While this statement is of course true in terms of whether the existence of the pledge transaction is susceptible to objective proof, it begs the question of whether a pledge, which does not involve the transfer of title or ownership, is nonetheless a "sale."

[6] Prudent and normal banking procedures mandate that the overall financial health of the borrower—not the existence of collateral—should be the first and most important criterion in decisions to extend credit.

support for the decision below than the court's own mistaken view of the nature of a pledge.

Guild Films involved a scheme by a bank and its debtor to distribute unregistered securities to the public and utilize the proceeds to satisfy a pre-existing debt. The district court found as fact that the "pledge" to the bank was a subterfuge sale to avoid the registration requirements of the 1933 Act and rightly enjoined the distribution at the instance of the SEC. 178 F. Supp. 418, 424 (S.D.N.Y. 1959). The court of appeals unnecessarily went much further, however, and asserted that all pledges of unregistered securities would be deemed "sales" for the purpose of distribution and all pledgees deemed statutory underwriters.[7] 279 F.2d at 489-90.

Guild Films has been roundly criticized regarding both its requirement of registration by pledgees[8] and its dictum as to pledges being sales.[9] Most lower courts con-

[7] Guild Films relied on the statutory definition in § 2(3), 15 U.S.C. § 77b(3), which defines "sale" as including "every . . . disposition of a security or interest in a security, for value," which is broader language than the 1934 Act definition. 279 F.2d at 489. *See Blue Chip Stamps*, *supra* at 733 n.5. But, as with the definition of "sale" in the 1934 Act, there is no indication of a congressional intent to alter the ordinary meaning of the word "sale" to include pledge transactions.

[8] *See* 1 L. Loss, Securities Regulation 645-51 (2d ed. 1961); Pierce, *Securities and Exchange Commission* v. *Guild Films Co. Inc.*, 16 Bus. Law. 603 (1961), citing Throop & Lane, *Some Problems of Exemption Under the Securities Act of 1933*, 4 Law & Contemp. Prob. 89, 124 (1937). *But see SEC* v. *Dolnick*, 501 F.2d 1279, 1283 (7th Cir. 1974); *SEC* v. *National Bankers Life Ins. Co.*, 334 F. Supp. 444, 456 (N.D. Tex. 1971), *aff'd*, 477 F.2d 920 (5th Cir. 1973).

[9] *See Investment Properties Int'l, Ltd.* v. *I.O.S. Ltd.*, [1970-1971] Fed. Sec. L. Rep. (CCH) ¶ 93,011 (S.D.N.Y. 1971):

"[P]laintiffs argue that the pledge should be deemed a 'sale,' and that the pledgee is a 'purchaser' for purposes of § 10(b)

(footnote continued)

sequently have declined to extend *Guild Films* to hold that a pledge is a "sale" for purposes of § 10(b) of the 1934 Act.[10]

The other case relied upon by the court below, *United States* v. *Gentile*, held that a pledge constituted a "sale" for the purpose of criminal prosecution under § 17(a) of the 1933 Act The *Gentile* opinion noted that *Guild Films* was "primarily intended to protect investors," but

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and Rule 10b-5. For this proposition plaintiffs rely upon *SEC* v. *Guild Films* . . ."

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"The uncertain scope of Guild Films has been noted. *See Fox* v. *Glickman Corporation*, 253 F. Supp. 1005, 1011-12 (S.D.N.Y. 1966), and authorities cited therein. This court concludes that where the pledgee seeks the label of "purchaser" for its own advantage rather than the satisfaction of some regulatory protection of others, where the collateral is taken at the initial making of the loan in circumstances suggesting that there was no initial intent to foreclose on the pledge or effect a distribution, and where there has in fact been no foreclosure and no attempt at distribution, the mere pledge of the shares of a foreign corporation is not a purchase or sale of securities within the context of § 10(b)."

[10] While lower courts have found varied bases to dismiss the claims, their analyses suffer from having to contend with the overbroad language of *Guild Films*. *See McClure* v. *First National Bank of Lubbock, Texas*, 497 F.2d at 495-96 (holding that a pledge itself is not a "sale" but reserving decision as to whether a sale out of pledge to a third party might be a "sale" as between pledgor and pledgee):

"A commercial bank's business is lending money not trading in securities. . . . [M]ere acceptance of a stock pledge as collateral in a privately negotiated transaction between borrower and lender does not, of itself, bring within the scope of the federal securities acts a transaction otherwise outside their purview."

Herpich v. *Wallace*, 430 F.2d 792, 811-12 (5th Cir. 1970) (*Guild Films* has no applicability under § 10(b)); *Bronner* v. *Goldman*, 361 F.2d 759, 762 (1st Cir.), *cert. denied*, 385 U.S. 933 (1966) (*Guild Films* applies only to definition of underwriter under 1933 Act); *Devonbrook, Inc.* v. *Lilly Lynn, Inc., supra* (no action under Rule 10b-5 by pledgor because no possible causal link); *Rosen* v. *Dick*, [1974-1975 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 94,786 at 96,605 (S.D.N.Y. 1974) (pledge not a "sale"; sale out of pledge upon default is a sale).

based its holding on the extraordinary, unsupported assertion that "there is no reason to doubt that Congress intended that Act to protect defrauded lenders just as much as defrauded buyers." 530 F.2d at 467.

Thus, neither of the decisions relied upon by the court below was based on analysis more substantial or persuasive than its own so far as § 10(b) of the 1934 Act is concerned. The absence of a reasoned basis for the decision below is finally and most clearly manifested by its internal contradiction. With respect to other defendants, the court held that plaintiffs could not invoke § 7 of the 1934 Act and Regulation U thereunder *because plaintiffs, as pledgees, did not "purchase" any stock—precisely the opposite of the holding reached later in the opinion as to plaintiffs' status under § 10 (b).* The 1934 Act's definition of "purchase" applies equally to § 7 and § 10(b), and if a pledge is not a "purchase" under § 7 it is not a "purchase" under § 10(b).

Conclusion

For the reasons stated, the judgment should be reversed.

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August 18, 1977